

Year-End Tax Planning
By Amy Boyd, 5500TaxGroup, Inc.

The end of 2007 is just around the corner, and now is a good time to start your year-end planning, especially with regard to your company's employee benefit plans.

Retirement Plans

Companies that do not have a retirement plan should consider adopting a plan before the end of the year. This will allow them to make contributions at any time up to the due date, including extension, of the business's tax return. The company may also be able to claim a general business tax credit for part of the ordinary and necessary costs of starting the plan. For an existing retirement plan, the company would do well to make sure that it is not only up-to-date with current law, but takes advantage of current changes in the law.

Starting in 2008, the Pension Protection Act allows companies to automatically enroll every employee in a 401(k) plan. This means that an employee has to actively opt out of the company's 401(k) plan or be automatically enrolled and contribute 3% of salary in the first year and an additional 1% every year after that (until maxing out at 6 to 10% of income). Plans implementing automatic enrollment will help employees save more for retirement. In addition, 401(k) plans will not be subject to the nondiscrimination testing, which is performed each year to ensure that highly-compensated employees do not benefit more in the 401(k) plan than non-highly compensated employees. Most companies' plan documents will need to be amended to allow for automatic enrollment.

Employees should also check their year-to-date contributions to retirement plans to be sure that they are maximizing their pre-tax contributions. The deductible maximum for 2007 is \$15,500. Employees changing their contribution deferral percentage will increase their retirement savings as well as reduce their taxable income for their 2007 tax return. Employees who turn age 50 in 2007, even on the last day of the year, can take advantage of an additional \$5,000 "catch-up" contribution. However, the company-sponsored retirement plan must allow for catch-up contributions.

Flexible Spending Accounts

Employer-sponsored Flexible Spending Accounts ("FSA") allow employees to set aside pre-tax money to pay out-of-pocket medical and child care expenses. These plans also allow employees and employers to reduce payroll taxes because monies withheld pre-tax are exempt from FICA and FUTA taxes.

Employees who make pre-tax contributions to their employer's flexible spending account should review their remaining balance before year's end. If they leave a balance in their account at year's end, they will lose the money. Purchasing new eye glasses or contacts, filling prescriptions earlier, or having dental work done are all great ways to utilize the funds in their account balance.

Employees should also review how much they will need to contribute for 2008 medical or dependent care expenses. A review of the previous year's expenses as well as an evaluation of the upcoming year's expenses will help determine how much the employee should have withheld. A child attending kindergarten in the fall will decrease their dependent child care expenses. Orthodontic and vision expenses will increase medical spending expenses. A few calculations now could mean substantial out-of-pocket and tax savings next year.

In 2005, the Internal Revenue Service changed the rules to allow participants to make claims against their accounts for up to 2 ½ months after the end of their benefit year. That means employees can now use their 2007 FSA contributions for expenses incurred as late as March 15, 2008. However, the employer's FSA plan must include the provisions for the extended date for withdrawals – otherwise, all expenses must be incurred before year's end.

Retirement Distributions

An individual must receive a certain minimum amount of their account balance by April 1st of the calendar year following the later of (1) the calendar year in which the employee becomes age 70 ½ or (2) the calendar year in which an employee retires. It is advisable to begin these distributions in the year the individual turns 70 ½ to avoid having to take two distributions the following year. After that, the required minimum distributions must be withdrawn from the retirement account before December 31st of each year.

Failure to take the required minimum distribution can be subject to an IRS penalty of up to 50 percent of the amount not withdrawn.

The *BRC will be presenting an educational seminar on Year-End Tax Planning, "Preparing Your Company and Your Employees for 2008", featuring Amy Boyd of the 5500TaxGroup, Inc. For more information about employee benefit consulting services, contact Amy Boyd at 5500Tax Group, Inc. by phone at (951)784-5316 or by email at amy.boyd@5500tax.com.

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